UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

No. 05-1774
November 8, 2006, Decided

ALAN NISSELSON, TRUSTEE OF THE DICTAPHONE LITIGATION TRUST,

Plaintiff-Appellant,

—v.—

JO LERNOUT *et al.*,

Defendants-Appellees.

Max Folkenflik and Regina Griffin, with whom Folkenflik & McGerity, Brauner Baron Rosenzweig & Klein, Karen D. Hurvitz, and Law Offices of Karen D. Hurvitz were on brief, for appellant.

George A. Zimmerman, with whom Matthew J. Matule and Skadden, Arps, Slate, Meagher & Flom LLP were on brief, for appellee SG Cowen and Company, LLC.

Janet B. Fierman, with whom Thomas W. Evans, Robert M. Cohen, and Cohen & Fierman, LLP were on brief, for appellee Mercator Assurances, S.A.

Robert J. Kaler, with whom Eric Neyman and Gadsby Hannah LLP were on brief, for appellees Flanders Language Valley Fund et al.

Michael P. Carroll, with whom Michael S. Flynn, Sean C. Knowles, Phineas E. Leahey, Davis Polk & Wardwell, Kevin J. Lesinski, William J. Hanlon, Kristin G. McGurn, and Seyfarth Shaw LLP were on brief, for appellee KPMG LLP.

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Michael J. Stone, Peabody & Arnold LLP, George A. Salter, Nicholas W.C. Corson, and Hogan & Hartson LLP on brief for appellee Klynveld Peat Marwick Goerdeler Bedrijfsrevisoren.

Robert P. Trout, John Thorpe Richards, Jr. and Trout Cacheris, PLLC on brief for appellee Lessius Management Consulting, N.V.

Andrew Good, Good & Cormier, Roger E. Zuckerman, Steven M. Salky, P. Andrew Torrez, and Zuckerman Spaeder LLP on brief for appellee Louis-H. Verbeke.

Before Selya, Lipez and Howard, Circuit Judges.

OPINION:

SELYA, Circuit Judge.

This appeal requires us to explore an arcane corner of the world of corporate finance. In the underlying series of events, a corporate shark, using fraudulent means, induced an allegedly innocent target corporation to enter into an ill-advised merger. After both the shark and the merged entity drowned in red ink, plaintiff-appellant Alan Nisselson (the trustee), appointed by the bankruptcy court to prosecute any causes of action that the merged entity might possess, attempted to mount various claims arising out of the innocent target's legal rights. Those rights, of course, were twice removed from the damages that formed the basis of the suit: they were passed along once to the surviving corporation (at the time of the merger) and again to the trustee (during the bankruptcy proceedings).

Emphasizing this genealogy, the district court dismissed the action on two grounds; it determined that the trustee lacked standing to pursue the claims and that, in all events, the rascality of the shark was as a matter of law imputed to the surviving entity in the merger (and that, therefore, the hoary in pari delicto doctrine barred the suit). See *Nisselson v. Lernout, No. 03-10843, 2004 U.S. Dist. LEXIS 28655, at *20-21 (D. Mass. Aug. 9, 2004)*. Concluding, as we do, that the second of these determinations withstands scrutiny—the trustee's claims are incurably tainted because they derive from the itself-complicit surviving corporation—we affirm the judgment below.

I. BACKGROUND

We glean the pertinent facts from the amended complaint, supplementing those facts as needed by docu-

ments fairly incorporated therein and matters susceptible to judicial notice. See *Centro Medico del Turabo, Inc. v. Feliciano de Melecio*, 406 F.3d 1, 5 (1st Cir. 2005); *In re Colonial Mortg. Bankers Corp.*, 324 F.3d 12, 15-16 (1st Cir. 2003). While the scheme that lies at the center of this case comprises a complex tale of sophisticated financial chicanery, we rehearse here only those features essential to an understanding of the present proceeding. We urge the reader who thirsts for greater knowledge to consult the array of published opinions emanating from related litigation. See, e.g., *Baena v. KPMG LLP*, 453 F.3d 1 (1st Cir. 2006); *Quaak v. Klynveld Peat Marwick Goerdeler Bedrijfsrevisoren*, 361 F.3d 11 (1st Cir. 2004); *Bamberg v. SG Cowen*, 236 F. Supp. 2d 79 (D. Mass. 2002); *Filler v. Lernout*, 230 F. Supp. 2d 152 (D. Mass. 2002); *In re Lernout & Hauspie Sec. Litig.*, 208 F. Supp. 2d 74 (D. Mass. 2002).

By the time the new millennium dawned, Dictaphone Corporation (Old Dictaphone), a company chartered under the laws of Delaware, had established itself as a force in the healthcare speech and language applications market. Lernout & Hauspie, N.V. (L&H), a Belgian corporation that ran its United States operations from headquarters in Massachusetts, was itself an international leader in various speech and language sectors. In hopes of swallowing up its competitor, L&H began courting Old Dictaphone; it described in glowing terms its financial stability and the profitable synergies that a merger could generate. Negotiations ensued.

Not surprisingly, Old Dictaphone conducted extensive due diligence investigations into L&H's fiscal health. During the course of that review, L&H's senior officers, investment bankers, attorneys, and auditors touted its financial prowess. Against this rose-colored backdrop, Old Dictaphone agreed to a stock-for-stock merger. The

parties memorialized the terms in a merger agreement dated March 7, 2000.

The merger took place less than two months thereafter: L&H acquired all the outstanding stock of Old Dictaphone in exchange for approximately 9,400,000 shares of L&H common stock. Based on the trading price of L&H stock at the time of the closing, the exchange corresponded to a merger price of roughly $930,000,000.

As part and parcel of the transaction, Old Dictaphone merged into Dark Acquisition Corp. (Dark), a wholly-owned subsidiary of L&H created under Delaware law for the express purpose of effectuating the merger. L&H's chief executive officer, defendant-appellee Gaston Bastiaens, doubled in brass as Dark's chief executive and lone director. He also signed the merger agreement on its behalf.

Under the terms of the merger agreement, Dark inherited Old Dictaphone's assets (including any existing legal claims) and assumed Old Dictaphone's liabilities. This arrangement corresponded to the dictates of Delaware law. See *Del. Code Ann. tit. 8, § 259(a)*. Dark survived the merger and Old Dictaphone ceased to exist. Dark then changed its name to Dictaphone Corporation (New Dictaphone).

The honeymoon was brief. Shortly after the merger had been consummated, L&H announced that the financial picture it had painted and displayed was not an accurate portrayal. As matters turned out, nearly two-thirds of L&H's reported revenue from 1998 through mid-2000 had been improperly recorded, so that an apparent $ 70,000,000 net profit for that period was in fact a net loss of a similar magnitude. The price of L&H shares plummeted and, on November 29, 2000, L&H and

New Dictaphone filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code.

We fast-forward to New Dictaphone's approved plan of reorganization. As part of that plan, the corporation conveyed its interest in any claims arising out of the merger to the Dictaphone Litigation Trust (the Trust). That assignment galvanized this suit: acting on behalf of the Trust, the trustee filed a civil action in federal district court seeking damages to compensate for the "loss or diminution of [Old Dictaphone's] value as a going concern."

The trustee's amended complaint characterizes the gross misstatments of earnings as the mainspring of a fraudulent scheme designed to inflate the value of L&H's stock. As the trustee envisions it, this scheme, which played out over a four-year period, was concocted and executed by the defendants in this case (who include the officers, directors, investment bankers, attorneys, and auditors of L&H, and divers entities related to them). The fallout from it rendered worthless the consideration that Old Dictaphone and its shareholders received (assumption of Old Dictaphone's debt and shares of L&H stock).

In his amended complaint, the trustee asserts federal securities and racketeering claims, see *15 U.S.C. §§ 78j(b), 78t(a); 18 U.S.C. § 1962(c); 17 C.F.R. § 240.10b-5*, as well as supplemental state-law claims for fraud, unfair trade practices, negligent misrepresentation, and conspiracy. The theory underlying each and all of these initiatives is that L&H, through its senior management, knowingly engaged in a scheme to classify research and development expenditures as fictional revenue in order to inflate the value of the company's stock. Then, knowing that they were selling a lie, L&H's hierarchs flaunted the company's ever-increasing stock price and used its apoc-

ryphal earnings to persuade Old Dictaphone and its shareholders to enter into a stock-for-stock merger. L&H relied on its investment bankers, attorneys, accountants, and related entities to substantiate its false claims; those parties, the trustee contends, knew that L&H was spinning a yarn, yet assisted it in perpetrating the fraud.[1]

Various defendants, led by SG Cowen (an investment banking house), filed motions to dismiss. See *Fed. R. Civ. P. 12(b)(6)*. All of these motions argued, in relevant part, that the trustee lacked standing and that his claims were barred under the in pari delicto doctrine. Some of the motions advanced additional grounds for dismissing particular claims. The trustee vigorously opposed the motions.

In due course, the district court granted Cowen's motion and dismissed the trustee's federal claims against Cowen with prejudice. See *Nisselson, 2004 U.S. Dist. LEXIS 28655, at *20-21*. The court rested its decision on two alternative grounds. First, it concluded that the in pari delicto doctrine barred the claims because the trustee had inherited them from New Dictaphone, an entity itself implicated in the alleged fraud. See *2004 U.S. Dist. LEXIS 28655, at *12-15*. Second, interpreting and applying the Delaware standard for distinguishing direct and derivative claims, it concluded that the trustee lacked standing because the claims asserted belonged to

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[1] This suit comprised one of many filed in the wake of L&H's revenue restatement. In one such related action, Stonington Partners, Inc., which had owned ninety-six percent of Old Dictaphone prior to the merger, sued for damages allegedly incurred when it traded its once-valuable interest for what ended up being worthless paper.

For his part, the trustee has brought separate actions for breach of fiduciary duty against Old Dictaphone's former directors and controlling shareholders and for breach of contract and negligence against the accountants and investment bankers who counseled Old Dictaphone during the merger negotiations.

Old Dictaphone's former shareholders, not to Old Dictaphone itself. See *2004 U.S. Dist. LEXIS 28655, at *15-20* (discussing, inter alia, *Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031, 1033 (Del. 2004)*). For the same reasons, the court, in a series of subsequent orders, granted the other appellees' motions to dismiss.[2] This timely appeal followed.

II. ANALYSIS

We review *Rule 12(b)(6)* dismissal orders de novo, assuming the truth of all well-pleaded facts contained in the operative version of the complaint and indulging all reasonable inferences in the plaintiff's favor. See *McCloskey v. Mueller, 446 F.3d 262, 266 (1st Cir. 2006)*. Facts distilled in that fashion may be augmented by reference to (i) documents annexed to it or fairly incorporated into it, and (ii) matters susceptible to judicial notice. See *Centro Medico del Turabo, 406 F.3d at 5*; *Rodi v. S. New Eng. Sch. of Law, 389 F.3d 5, 12 (1st Cir. 2004)*. Where, as here, a district court rests its decision on alternative grounds, an appellate court need not explore both; if it determines that one such ground fully supports the order of dismissal, the court may end its deliberations at that point. See *Feinstein v. Resolution Trust Corp., 942 F.2d 34, 41 n.7 (1st Cir. 1991)*.

This case presents an idiosyncratic procedural feature. While most *Rule 12(b)(6)* motions are premised on a plaintiff's putative failure to state an actionable claim, such a motion may sometimes be premised on the inevitable success of an affirmative defense. See, e.g., *In re Colonial Mortg. Bankers, 324 F.3d at 16*; *Blackstone Realty v. FDIC, 244 F.3d 193, 197 (1st Cir. 2001)*; *Keene*

[2] The lower court did not reach any of the additional arguments proffered by the defendants, nor do we.

Lumber Co. v. Leventhal, 165 F.2d 815, 820 (1st Cir. 1948). Dismissing a case under *Rule 12(b)(6)* on the basis of an affirmative defense requires that "(i) the facts establishing the defense are definitively ascertainable from the complaint and the other allowable sources of information, and (ii) those facts suffice to establish the affirmative defense with certitude." *Rodi, 389 F.3d at 12.*

A. Standing.

The district court characterized both the in pari delicto doctrine and the absence of cognizable injury as evincing a lack of standing. See *Nisselson, 2004 U.S. Dist. LEXIS 28655, at *12-13*. Part of this characterization is inapt: the in pari delicto doctrine does not implicate a plaintiff's standing to sue but, rather, constitutes an affirmative defense. See *Official Comm. of Unsecured Creditors of PSA, Inc. v. Edwards, 437 F.3d 1145, 1149-50 (11th Cir. 2006)*; *Official Comm. of Unsecured Creditors of Color Tile, Inc. v. Coopers & Lybrand, LLP, 322 F.3d 147, 157 (2d Cir. 2003)*; see also *Baena, 453 F.3d at 6* (noting that the doctrine is, on occasion, "dubiously" referred to as implicating standing).

This does not mean, however, that we must grapple with the district court's alternative "distinct injury" holding first. Even though challenges to a plaintiff's standing are often considered threshold issues in federal cases, see, e.g., *Pagan v. Calderon, 448 F.3d 16, 26 (1st Cir. 2006)*; *Eulitt v. Me. Dep't of Educ., 386 F.3d 344, 351 (1st Cir. 2004)*, such challenges must be addressed first only if they call into question a federal court's Article III power to hear the case. See *Steel Co. v. Citizens for a Better Env't, 523 U.S. 83, 94-95, 118 S. Ct. 1003, 140 L. Ed. 2d 210 (1998)*. The constitutional prerequisites for Article III standing are satisfied so long as a plaintiff colorably alleges an actual injury that is both

traceable to the defendant's conduct and redressable by a favorable decision. See *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 560-62, 112 S. Ct. 2130, 119 L. Ed. 2d 351 (1992); *Ramirez v. Sanchez Ramos*, 438 F.3d 92, 97 (1st Cir. 2006).

In this case, those prerequisites have been fulfilled. For purposes of their motions to dismiss, the defendants wisely choose not to contest the trustee's assertion that the conduct attributed to them resulted in a redressable injury; instead, they posit that the trustee is seeking to prosecute claims that, although cognizable in a federal court, belong exclusively to Old Dictaphone's former shareholders. The determination of who may maintain an otherwise cognizable claim turns on a question of prudential standing, not one of Article III standing. See *Baena*, 453 F.3d at 5; see also *Ramirez*, 438 F.3d at 98.

That frees our hands: Steel Co.'s ban on hypothetical jurisdiction extends only to issues involving Article III jurisdiction and, hence, Article III standing. There is no counterpart rule that demands the resolution of objections based on prudential concerns before other issues can be adjudicated. See *Baena*, 453 F.3d at 5; *McBee v. Delica Co.*, 417 F.3d 107, 127 (1st Cir. 2005).

Mandatory rules aside, courts should not rush to rely on hypothetical jurisdiction. See *Berner v. Delahanty*, 129 F.3d 20, 23 (1st Cir. 1997). Nevertheless, one situation in which hypothetical jurisdiction, if otherwise proper, may be invoked is when doing so would avoid the need to sort out thorny jurisdictional tangles. See, e.g., *McBee*, 417 F.3d at 127; *Parella v. Ret. Bd. of R.I. Employees' Ret. Sys.*, 173 F.3d 46, 56 (1st Cir. 1999). As we explain briefly, just such a tangle exists here.

Although the decision in Tooley may have helped to clarify the often elusive distinction between direct and derivative claims, that distinction remains tenebrous. See

Richard Montgomery Donaldson, Mapping Delaware's Elusive Divide: Clarification and Further Movement Toward a Merits-Based Analysis for Distinguishing Derivative and Direct Claims in Agostino v. Hick and Tooley v. Donaldson, Lufkin & Jenrette, Inc., *30 Del. J. Corp. L. 389, 404 (2005)* (listing the "determination of who suffered the harm—the corporation or the shareholder(s)" as one of the potentially confusing issues left open under Tooley). More to the point, it is not immediately apparent how the Delaware court's newly announced two-part test, *845 A.2d at 1033*, should apply to the unique facts of this stock-for-stock merger. Because the record reflects a clear and sufficient basis apart from standing for affirming the district court's judgment, we bypass these uncharted waters.

B. The In Pari Delicto Doctrine.

In pari delicto is both an affirmative defense and an equitable defense. Broadly speaking, the defense prohibits plaintiffs from recovering damages resulting from their own wrongdoing. See *Terlecky v. Hurd (In re Dublin Sec.), 133 F.3d 377, 380 (6th Cir. 1997)*. The label derives from the Latin phrase in pari delicto potior est conditio possidentis, which admonishes that "[i]n a case of equal or mutual fault . . . the condition of the [defending party] is the better one." Black's Law Dictionary 791 (6th ed. 1990).

The doctrine is grounded on twin premises. The first is that "courts should not lend their good offices to mediating disputes among wrongdoers." *Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 306, 105 S. Ct. 2622, 86 L. Ed. 2d 215 (1985)*. The second is that "denying judicial relief to an admitted wrongdoer is an effective means of deterring illegality." Id.

The in pari delicto defense has long been woven into the fabric of federal law. See *id. at 307* (discussing the doctrine's historical development); see also *Fleming v. Lind-Waldock & Co., 922 F.2d 20, 28 (1st Cir. 1990)*; *Duncan v. Maine C. R. Co., 113 F. 508, 509 (C.C.D. Me. 1902)*. It does not make a difference that some of the trustee's claims are premised on state law. Those claims invoke the law of Massachusetts—and the Massachusetts courts, like the federal courts, have warmly embraced the in pari delicto defense. See, e.g., *Council v. Cohen, 303 Mass. 348, 21 N.E.2d 967, 970 (Mass. 1939)*; *Choquette v. Isacoff, 65 Mass. App. Ct. 1, 836 N.E.2d 329, 332 (Mass. App. Ct. 2005)*.

As originally conceived, the in pari delicto doctrine forged a defense of limited utility. Over time, however, courts expanded the doctrine's sweep, deploying it as a basis for dismissing suits whenever a plaintiff had played any role—no matter how modest—in the harm-producing activity. See *Bateman Eichler, 472 U.S. at 307*. Deploring this overly commodious construction, the Supreme Court later reined in the doctrine and returned it to its classic contours. See *Pinter v. Dahl, 486 U.S. 622, 635, 108 S. Ct. 2063, 100 L. Ed. 2d 658 (1988)*; *Bateman Eichler, 472 U.S. at 310-11*. This retrenchment, which governs here, restricts the application of the in pari delicto doctrine to those situations in which (i) the plaintiff, as compared to the defendant, bears at least substantially equal responsibility for the wrong he seeks to redress and (ii) preclusion of the suit would not interfere with the purposes of the underlying law or otherwise contravene the public interest. See *Bateman Eichler, 472 U.S. at 311* (discussing the doctrine's application to federal securities laws); see also *Edwards, 437 F.3d at 1154*. Recent Massachusetts case law mirrors

these refinements. See, e.g., *Choquette, 836 N.E.2d at 332-33.*

While the application of this binary paradigm may vary slightly depending on the nature of the particular claim asserted, courts nonetheless speak of a single doctrine. This is because the analysis ordinarily will be the same across a spectrum of different causes of action. See *Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co., 267 F.3d 340, 345-46 (3d Cir. 2001)*; see also *Coopers & Lybrand, 322 F.3d at 160.*

The court below adopted this one-size-fits-all approach in addressing the in pari delicto defense; it neither distinguished among the various counts nor differentiated between federal and state law. The trustee has not objected to this approach, so he has waived any argument either that a claim-by-claim analysis is obligatory or that some material differences exist between applicable federal and state law. See *Domegan v. Fair, 859 F.2d 1059, 1065 (1st Cir. 1988)* ("It is too familiar to warrant string citation that we will not consider arguments which could have been, but were not, advanced below."). Consequently, we employ the same generic strain of the in pari delicto doctrine throughout our review.

C. Establishing the Appropriate Benchmark.

To apply the requisite two-part paradigm in the circumstances of this case, we must answer a threshold question: Who, exactly, are the proper parties for the purpose of determining relative blame? The trustee's answer to this query is straightforward. Because his claims originate with Old Dictaphone, he asseverates that this indisputably innocent party is the relevant entity for purposes of the comparison required by the binary in pari delicto test. Since Old Dictaphone was the

victim rather than a perpetrator of the alleged fraud, the trustee's thesis runs, it bears less responsibility than any of the defendants and, therefore, the defendants fail to satisfy the first precondition for use of the in pari delicto defense. On that basis, the trustee claims an entitlement to recover for the injury that Old Dictaphone suffered when it was duped into proceeding with the merger.

We assume, for argument's sake, that Old Dictaphone would have been a proper party to sue for the asserted injury. See supra Part II (A). Even so, the trustee's reasoning is flawed; his analysis entirely overlooks that, pursuant to both the merger agreement and the governing law, see *Del. Code Ann. tit. 8, § 259(a)*, upon the consummation of the merger Old Dictaphone vanished into thin air and New Dictaphone inherited all of Old Dictaphone's choses in action. Under the approved plan of reorganization incident to New Dictaphone's bankruptcy, those litigation rights were passed along once more—this time to the Trust (and, thus, to the trustee). See *11 U.S.C. § 541(a)(1)*. Because the lineage of the trustee's claims passes directly through New Dictaphone, any right that the trustee may have to assert those claims derives directly from New Dictaphone. This chain of descent means that the trustee—despite his protestations to the contrary—is not acting in the place and stead of Old Dictaphone but, rather, in the place and stead of New Dictaphone.

This genealogy is important. Giving effect to it, the trustee may assert only those claims that New Dictaphone could have asserted prior to seeking the protection of the bankruptcy court. See *Mediators, Inc. v. Manney (In re Mediators, Inc.), 105 F.3d 822, 826 (2d Cir. 1997)*; see also *11 U.S.C. § 541*. After all, a trustee in bankruptcy cannot and does not acquire rights or interests superior to, or greater than, those possessed by the

debtor. See *Edwards, 437 F.3d at 1150*; 5 *Collier on Bankruptcy § 541.04* (15th ed. 2006) (noting that "nothing in *section 541* [of the Bankruptcy Code, defining property of the estate] can revest a debtor with property lost prepetition" and describing property of the estate as including "causes of action").

Given the line of descent delineated by operation of the corporation and bankruptcy laws, we think that the in pari delicto defense must be available to a defendant in an action by a bankruptcy trustee whenever that defense would have been available in an action by the debtor. See *Edwards, 437 F.3d at 1152*; see also *Baena, 453 F.3d at 7* (assessing the debtor's culpability to determine whether the in pari delicto doctrine barred a bankruptcy trustee's claims). As a necessary corollary of that proposition, there is no "innocent successor" exception available to a bankruptcy trustee in a case in which the defendant successfully could have mounted an in pari delicto defense against the debtor. See *R.F. Lafferty, 267 F.3d at 356-57*.

The explication of these principles suffices to answer the threshold question here. Consistent with both precedent and analytic rigor, we hold that New Dictaphone is the relevant comparator vis-a-vis the defendants for the purpose of determining the viability of the latter's in pari delicto defense. Old Dictaphone's innocence is irrelevant to that inquiry.

D. Applying the Paradigm.

Having determined that New Dictaphone is the entity of interest for purposes of the required comparison, we move to the question of what actions can, at this stage of the proceedings, be imputed to it (and, thus, to the trustee). See *Baena, 453 F.3d at 7*. In an effort to mount a preemptive strike, the trustee posits that because all

imputation inquiries entail fact-specific determinations, an in pari delicto defense that relies on imputed conduct cannot be adjudicated on a motion to dismiss. Although the trustee's premise is partially correct—the extent to which fraudulent conduct can be implied depends heavily on the specific facts of a given case—he casts the net too wide.

The reporters are replete with examples of fact-dominated questions, normally grist for the jury's mill, that may appropriately be resolved by a motion filed pursuant to *Rule 12(b)(6)*. See, e.g., *Epstein v. C.R. Bard, Inc., 460 F.3d 183, 188 (1st Cir. 2006)*; *Rodi, 389 F.3d at 16*. The key is whether the factual scenario, as pleaded, is clear enough to permit peremptory resolution of the dispositive issue. See *Rodi, 389 F.3d at 16* (explaining that when the facts alleged in the complaint preclude a finding in the plaintiff's favor on a particular claim or defense, "a court may enter an order of dismissal under *Rule 12(b)(6)*"). When a case hinges on imputation and the pleaded facts, construed in the light most flattering to the resisting party, dictate imputation, a court is free to decide that question on a motion to dismiss. See, e.g., *Baena, 453 F.3d at 8* (affirming dismissal on in pari delicto grounds after imputing fraudulent conduct to debtor corporation); *Coopers & Lybrand, 322 F.3d at 164*; (noting that the court historically "has affirmed the dismissal of . . . claims on the pleadings upon findings that in pari delicto had been established in the complaints"); *Terlecky, 133 F.3d at 380* (affirming dismissal when the debtor "admit[ted] in his complaint that the debtor's own actions were instrumental in perpetrating the fraud").

We look to state law to ascertain when wrongful conduct should be imputed to a corporation. See *O'Melveny & Myers v. FDIC, 512 U.S. 79, 84, 114 S. Ct. 2048, 129*

L. Ed. 2d 67 (1994); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Nickless (In re Advanced RISC Corp.), 324 B.R. 10, 14 (D. Mass. 2005)*.[3] Here, the case law leaves little doubt that Massachusetts law governs the imputation calculus. See *O'Melveny & Myers, 512 U.S. at 83-85* (emphasizing the importance of the substantive law of the state in which the causes of action arose, rather than the law of the state of incorporation, to determine imputation).

Under Massachusetts law, a parent and its wholly-owned subsidiary are generally regarded as separate and distinct entities. See *United Elec., Radio & Mach. Workers v. 163 Pleasant St. Corp., 960 F.2d 1080, 1091 (1st Cir. 1992)*; *Berger v. H.P. Hood, Inc., 416 Mass. 652, 624 N.E.2d 947, 950 (Mass. 1993)*. Courts may, however, disregard the corporate form when doing so will defeat a fraud practiced by those who control the subsidiary corporation. See *My Bread Baking Co. v. Cumberland Farms, Inc., 353 Mass. 614, 233 N.E.2d 748, 751 (Mass. 1968)*. Relatedly, the fraudulent conduct of persons or entities who exercise complete control over a corporation may be imputed to the corporation when those actors have used the corporation as a vehicle for facilitation of the fraud. See, e.g., *Consove v. Cohen (In*

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[3] To the extent that the trustee's claims are premised on federal statutes, we arguably have discretion to use federal common law, as opposed to state law. See *O'Melveny & Myers, 512 U.S. at 84* (explaining that where a particular cause of action arises under a federal statute, a federal court, for this purpose, writes on a pristine page). Even so, license to apply a uniquely federal test is not tantamount to mandating such a test. Mindful that two of our sister circuits recently have opted for state-law tests of imputation in connection with federal claims, see *Edwards, 437 F.3d at 1149*; *R.F. Lafferty, 267 F.3d at 358*, and that no party to this litigation has requested us to fashion federal common law, we use Massachusetts jurisprudence as the yardstick for measuring imputation across the board.

re Roco Corp.), 701 F.2d 978, 984 (1st Cir. 1983) (applying Massachusetts law and imputing fraudulent conduct of individual who, "as the company's president, director, and sole shareholder, . . . was in a position to control the disposition of its property"); *Merrill Lynch, 324 B.R. at 14-15* (applying Massachusetts law and imputing principals' fraudulent conduct to debtor corporation where the relationship was "one of complete control"); *Demoulas v. Demoulas, 428 Mass. 555, 703 N.E.2d 1149, 1171 (Mass. 1998)* (applying Massachusetts law and denying bona fide purchaser status to a corporation, under an imputation theory, when the "sole voting trustee of 100 percent of the [corporation's] stock" had actual knowledge of adverse claims against the purchased property).

With this backdrop in place, the trustee's remaining arguments against imputing L&H's fraudulent conduct to its wholly-owned subsidiary lack force. The trustee himself has observed that in pari delicto cases often result in imputation of fraudulent conduct to a corporation when those responsible for the scheme are "the sole decision-maker[s] for such entity, exercising complete control over its management." Appellant's Br. at 43 n.21. This observation accurately reflects the case law. See, e.g., *Coopers & Lybrand, 322 F.3d at 164-65* (imputing fraudulent conduct to debtor when complaint established that its controlling shareholders "dominat[ed] and control[ed] the corporation" and were responsible for "orchestrat[ing] the fraudulent conduct"); *R.F. Lafferty, 267 F.3d at 359-60* (imputing fraudulent conduct to debtor corporation and dismissing trustee's case on in pari delicto grounds where the individuals masterminding the fraud were the debtor's sole shareholders); *Merrill Lynch, 324 B.R. at 14-16* (dismissing trustee's action on in pari delicto grounds when debtor corporation was

formed by the defrauders for the express purpose of carrying out the fraudulent plan). Since New Dictaphone, not Old Dictaphone, is the proper focal point of our imputation inquiry, see supra Part II (C), this case fits snugly within that integument. We explain briefly.

Here, the amended complaint leaves no doubt but that L&H played the primary role in contriving the scheme to acquire Old Dictaphone under false pretenses. The amended complaint also establishes that L&H created New Dictaphone (nee Dark) for the express purpose of furthering this artifice. L&H's control over New Dictaphone during the course of the scheme is indisputable. In addition to owning all of New Dictaphone's stock, L&H installed its president, Bastiaens, as New Dictaphone's chief executive officer and sole director. Bastiaens, in turn, ensured New Dictaphone's complicity in the fraud's climactic event when he executed the merger agreement on its behalf.

These uncontroverted facts are telling. Because the amended complaint shows beyond hope of contradiction that L&H created and controlled New Dictaphone in order to perpetrate the harm-producing fraud, we have no principled choice but to impute its conduct to New Dictaphone for the purpose of applying the in pari delicto paradigm. See *Merrill Lynch, 324 B.R. at 15*; *Demoulas, 703 N.E.2d at 1172*; *My Bread Baking, 233 N.E.2d at 751*.

The trustee tries to find sanctuary by pointing out that, after the merger, the directors of Old Dictaphone (presumably innocent) became directors of New Dictaphone. This datum does not alter our conclusion. The first prong of the in pari delicto inquiry focuses on "the unlawful activity that is the subject of the suit." *Pinter, 486 U.S. at 636*. Accordingly, a party's culpability vel non must be based on its status at the time the alleged illegality

occurred. See *Baena, 453 F.3d at 10* (finding no Massachusetts case law supporting a theory that in pari delicto is in any way modified when "prior management was at fault but the claim [is] asserted on behalf of creditors or shareholders").

Here, of course, the fraud that underpins the trustee's claims was complete at the moment the companies merged. Therefore, any post-merger changes in New Dictaphone's corporate governance or management are beside the point. Simply put, bankruptcy trustees do not have access to an "innocent successor" exception as a way of shielding themselves from the operation of an in pari delicto defense. See *R.F. Lafferty, 267 F.3d at 356-57*; see also *Baena, 453 F.3d at 10*.

The trustee's next attempt to elude the toils of the in pari delicto doctrine involves the well-recognized adverse interest exception. Generally, a wrongdoer's fraudulent acts will not be imputed to a corporation when the wrongdoer is acting contrary to the corporation's present interests. See, e.g., *Baena, 453 F.3d at 8* (listing looting as a "classic example" of adverse conduct); *Sunrise Props., Inc. v. Bacon, Wilson, Ratner, Cohen, Salvage, Fialky & Fitzgerald, P.C., 425 Mass. 63, 679 N.E.2d 540, 543 (Mass. 1997)* (concluding that "unauthorized acts [should] not [be] imputed to the principal when the agent has acted fraudulently toward the principal"). Endeavoring to squeeze within these narrow confines, the trustee contends that L&H's scurrilous conduct is tantamount to looting because L&H convinced Old Dictaphone to surrender its assets for worthless paper.

This contention is ill-conceived, for the trustee's sights are trained on the wrong entity. Accepting the allegations of the amended complaint as true, L&H's actions were adverse to Old Dictaphone and its share-

holders—but they were not adverse to New Dictaphone (a corporate shell which, in effect, was in league with the defrauder and as a result received something for nothing). Since we already have determined that New Dictaphone, not Old Dictaphone, is the focal point of the imputation inquiry, see supra Part II (C), the adverse interest exception does not apply.

The trustee has yet another string to his bow. He argues that even if New Dictaphone is the proper focal point of an in pari delicto analysis, the adverse interest exception precludes us from imputing L&H's fraud to its subsidiary because New Dictaphone was "entirely indifferent" about whether Old Dictaphone received fair value for its assets or whether L&H used skulduggery to effect the acquisition. Appellant's Reply Br. at 19. We find this argument unpersuasive. In our view, mere indifference is insufficient to show adversity. The adverse interest exception applies only to those whom the fraud has disadvantaged. See *Restatement (Second) of Agency § 282(1)* (explaining that the exception attaches only when an agent secretly acts adversely to his principal). In this instance, the allegations of the amended complaint make manifest that New Dictaphone benefitted from the fraud: it was the surviving entity in a merger that netted it over $ 900,000,000. New Dictaphone, as a beneficiary of L&H's chicanery at the time the fraud was consummated,[4] cannot rely on the adverse interest exception to avoid imputation. After all, a party cannot

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[4] Because the adverse interest exception turns on how the alleged wrongdoing affected the immediate interests of the party who seeks its shelter, New Dictaphone's subsequent implosion is of no moment. See *Baena, 453 F.3d at 7*; accord *Beck v. Deloitte & Touche, Deloitte, Haskins & Sells, Ernst & Young, L.L.P., 144 F.3d 732, 736 (11th Cir. 1998)* (applying Florida law); *Cenco Inc. v. Seidman & Seidman, 686 F.2d 449, 456 (7th Cir. 1982)* (applying Illinois law).

accept the avails of fraudulent conduct without also bearing responsibility for that conduct. See *Tremont Trust Co. v. Noyes, 246 Mass. 197, 141 N.E. 93, 98 (Mass. 1923)*.

To summarize succinctly, L&H was the main player in the alleged fraud and its parlous behavior must be imputed lock, stock, and barrel to its offspring (New Dictaphone). It follows inexorably that New Dictaphone, in contemplation of law, bears at least as much responsibility for the asserted wrongdoing as any of the defendants.[5] Hence, the moving defendants have satisfied the first requirement for establishing an in pari delicto defense.

We move next to the second requirement. As said, this prong implicates public policy concerns. The trustee contends that allowing the defendants to hide behind the in pari delicto doctrine would frustrate the purpose of the securities laws because it would allow participants in a fraudulent scheme to shield themselves from liability. This contention is wide of the mark.

As we have pointed out, the trustee is not bringing claims on behalf of an innocent target of the fraud but, rather, on behalf of a complicit party. Viewed in that light, the trustee's policy concerns ring hollow.[6] See *Edwards*,

[5] As a fallback, the trustee suggests that the relevant comparison entails matching New Dictaphone's culpability against the culpability of L&H. That suggestion is faulty. When deciding whether to recognize an in pari delicto defense, an inquiring court must consider whether the party alleging injury (here, the trustee, who stands in the shoes of New Dictaphone) bears substantially equal (or greater) responsibility as the party or parties asserting the defense (here, the defendants). See *Bateman Eichler, 472 U.S. at 306* (emphasizing the relative culpability of the "[defending] party" as compared to the plaintiff (alteration in original)). RL&H is not a defendant in this action.

[6] In all events, dismissing the claims at issue here will not allow the defendants to escape unscathed. The amended complaint and matters susceptible to judicial notice reveal that many of the

437 F.3d at 1155 (finding public policy exception inapplicable in analogous circumstances).

The trustee also asserts that withholding application of the in pari delicto doctrine would promote the goal of "discourag[ing] wrongdoers from engaging in future fraudulent schemes and violations of the securities laws." Appellant's Br. at 38. That resupinate reasoning turns reality on its head. To permit the trustee to proceed in these circumstances would be equivalent to giving New Dictaphone a second bite at the cherry, allowing it first to reap the benefits of the fraud and then to attack the defrauders. The securities laws were enacted to protect investors from deceptive practices, see *Pinter, 486 U.S. at 638*, not to give the intended beneficiaries of deceptive practices a back-door means of ensuring a profit.

Finally, the trustee strives to persuade us that we should repel the defendants' in pari delicto defense because, in the absence of that defense, the creditors of Old Dictaphone ultimately would receive the fruits of any recovery. We find this argument unconvincing; despite the interposition of the in pari delicto defense, the creditors remain free to proceed in their own right, untainted by New Dictaphone's role in the alleged wrongdoing. See *Edwards, 437 F.3d at 1151*; *Terlecky, 133 F.3d at 380*; *Merrill Lynch, 324 B.R. at 16*.

This arrangement is especially preferable because the Trust beneficiaries may well include parties (most notably L&H) who were themselves complicit in the underlying fraud. If we were to suspend the operation of the in pari delicto defense in this case, creditors with unclean hands would profit equally with innocents. If,

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defendants are facing or have faced not only criminal charges but also a myriad of other civil suits relating to their respective roles in the alleged fraud.

however, each creditor must proceed by individual suit, the righteous may recover while the tainted, unable to circumvent the in pari delicto bar, will be hoist by their own petard.

At oral argument, the trustee insisted that the alternative of direct suits by creditors is illusory because creditors lack contractual privity with the investment bankers, lawyers, and accountants who comprise the trustee's targets. Thus, the argument runs, if we afford these targets the safe haven of an in pari delicto doctrine, creditors will be completely foreclosed from accessing those pockets that are deep enough to compensate them at anything higher than pennies on the dollar.

This jeremiad is unavailing. Even assuming that the trustee's premise is true—and we have some doubt about its validity—the equities are not nearly so clear-cut. First, the creditors (or the trustee, on their behalf) may well succeed in suits against Old Dictaphone's former directors, controlling shareholder, and outside accounting professionals. See supra note 1. Second—and more important—our holding today breaks no new ground. As such, the potential for default under these circumstances is something about which creditors had notice—something that should have been priced into their decisions to extend credit. Equity does not require courts to provide a belt when creditors had fair warning that they ought to have purchased suspenders.

III. CONCLUSION

To summarize, we conclude that uncontroverted facts sufficient to establish the in pari delicto defense are definitively ascertainable from the amended complaint and other allowable sources of information. These include L&H's creation of New Dictaphone for the express purpose of effectuating the fraud-inspired

merger and its exercise of complete control over New Dictaphone until the fraud was consummated. In these circumstances, L&H's conduct must be imputed to New Dictaphone. Consequently, New Dictaphone shares the culpability of the fraud's progenitor and, as such, bears as much or more responsibility for the wrongdoing as any of the named defendants. In the absence of any compelling public policy reason to allow New Dictaphone to seek damages from those that assisted in executing the fraudulent scheme—and the trustee has identified none—the in pari delicto doctrine precludes New Dictaphone (and, hence, the trustee) from advancing the type of claims that are at issue here.

We need go no further. For the reasons elucidated above, we hold that the district court did not err in dismissing the trustee's amended complaint.

Affirmed.

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MASSACHUSETTS

CIVIL ACTION NO. 03-10843-PBS
August 9, 2004, Decided
August 9, 2004, Filed

ALAN NISSELSON, TRUSTEE OF THE DICTAPHONE LITIGATION TRUST,
Plaintiff,

—v.—

JO LERNOUT, *et al.*,
Defendant.

For Alan Nisselson, Trustee of the Dictaphone Litigation Trust, successor-in-interest to claims of Dictaphone Corporation, Plaintiff: Karen D. Hurvitz, Jamaica Plain, MA; Margaret McGerity, Folkenflik & McGerity, New York, NY; Max Folkenflik, Folkenflik & McGerity, New York, NY; Regina Griffin, Brauner, Baron, Rosenzweig & Klein LLP, New York, NY.

For Jo Lernout, Defendant: Anthony M. Feeherry, Goodwin Procter, LLP, Boston, MA; Gus P. Coldebella, Goodwin Procter, LLP, Boston, MA.

For Pol Hauspie, Nico Willaert, Defendants: Donald H. Chase, Morrison Cohen LLP, New York, NY; Edward P.

Gilbert, Morrison Cohen Singer & Weinstein, LLP, New York, NY; Gordon M. Jones, Nixon Peabody, LLP, Boston, MA; Robert P. Sherman, Nixon Peabody LLP (BOS), Boston, MA.

For Ellen Spooren, Defendant: Michael P. Connolly, Murtha Cullina LLP, Boston, MA.

For Erwin Vanderriessche, RVD Securities, Dick Cauweiler, Marc G.H. DePauw, Girard Van Acker, Defendants: Ada Fernandez Johnson, Debevoise & Plimpton, Washington, DC; John B. Missing, Debevoise & Plimpton, LLP, Washington, DC; Thomas J. Gallitano, Conn, Kavanaugh, Rosenthal, Peisch & Ford, LLP, Boston, MA.

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For Lessius Management Consulting, N.V., Defendant: John Thorpe Richards, Jr, Robert P Trout, Trout & Richards, PLLC, Washington, DC; Peter B. Krupp, Lurie and Krupp, LLP, Boston, MA.

For Gewestelike Investeringsmaatschappij Voor Vlaanderen N.V., Defendant: Thomas J. Gallitano, Conn, Kavanaugh, Rosenthal, Peisch & Ford, LLP, Boston, MA.

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For Paul Behets, Defendant: Caroline Press, Louis M. Solomon, Proskauer Rose, LLP, New York, NY; Michael J. Stone, Peabody & Arnold LLP, Boston, MA.

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For Chase Securities, Defendant: Dalila A. Wendlandt, Elizabeth Abimbola Thomas, John D. Donovan, Jr., Ropes & Gray LLP, Boston, MA.

For Deloitte & Touche, Defendant: Daniel A. Curto, McDermott, Will & Emery LLP, Boston, MA; Derek J.T. Adler, William R. Maguire, Hughes Hubbard & Reed, LLP, New York, NY; Edward P. Leibensperger, McDermott, Will & Emery, Boston, MA.

For Stonington Partners, Inc., Stonington Capital Appreciation 1994 Fund, L.P, Stonington Holdings, L.L.C., Albert J. Fitzgibbons, Emil F. Jachmann, Alexis P. Michas, Scott M. Shaw, Peter P. Tong, Defendants: Charles P. Kindregan, Looney & Grossman, Boston, MA; Gary J. Mennitt, Dechert LLP (NY), New York, NY.

For John H. Duerden, Defendant: Alan D. Rose, Sr, Michael L. Chinitz, Rose & Associates, Boston, MA; James G. McCarney, Thomas E. Engel, Engel & McCarney, New York, NY; Rupinder Hans, Engel & McCarney, New York, NY.

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Jonathan K. Cooperman, Kelley Drye & Warren, New York, NY; Peter E. Gelhaar, Jill Brenner Meixel, Donnelly, Conroy & Gelhaar, LLP, Boston, MA.

For Louis H. Verbeke, Defendant: Andrew Good, Good & Cormier, Boston, MA; Steven M. Salky, Zuckerman Spaeder LLP, Washington, DC; Roger E Zuckerman, Zuckerman Spaeder LLP, Washington, DC.

For Language Investment Company, Willem Hardeman, Defendants: Karen D. Hurvitz, Jamaica Plain, MA.

For KPMG Bedrijfsrevisoren, Defendant: Michael J. Stone, Peabody & Arnold LLP, Boston, MA.

For Mercator Assurances, S.A., Defendant: Janet B. Fierman, Cohen & Fierman, LP, Boston, MA; Thomas W. Evans, Cohen & Fierman, LLP, Boston, MA.

PATTI B. SARIS, United States District Judge.

OPINION:

MEMORANDUM AND ORDER

Saris, U.S.D.J.

I. INTRODUCTION

This case arises out of the stock-for-stock merger of Dictaphone Corporation ("Old Dictaphone") into a subsidiary of Lernout & Hauspie N.V. ("L&H"). An alleged fraudulent scheme at L&H rendered the L&H stock

worthless, and the shareholders sued.[1] Plaintiff Alan Nisselson, Trustee of the Dictaphone Litigation Trust, has filed a separate action alleging that Defendant SG Cowen Securities Corporation ("SG Cowen"), L&H's investment banker, participated in the scheme and defrauded Dictaphone by encouraging it to enter into the merger agreement. Specifically, plaintiff brings claims of common law fraud, unfair trade practices pursuant to *Mass. Gen. Laws. ch. 93A*, negligent mispresentation, conspiracy, and violations of RICO against SG Cowen. SG Cowen moves to dismiss the Amended Complaint in its entirety on the grounds that the Trustee lacks standing because only the shareholders have been injured by the drop in stock value, and the action is barred by the doctrine of in pari delecto. After hearing, the motion to dismiss is **ALLOWED.**

II. FACTUAL BACKGROUND[2]

The Amended Complaint alleges the following facts.

In early 2000, L&H and SG Cowen approached Dictaphone to discuss the possibility of acquiring Dictaphone—one of its major competitors in the speech and language applications sector. At that time, Stonington Fund was the owner of approximately 96% of the autho-

[1] See Stonington Partners, Inc. v. Dammekens, No. 02-10303-PBS (D. Mass. filed Feb. 21., 2002).

[2] This Court has written several extensive opinions concerning the alleged fraudulent scheme at L&H. Familiarity with the facts set out in those opinions is assumed. See, e.g., *In re Lernout & Hauspie Sec. Litig.*, *208 F. Supp. 2d 74 (D. Mass. June 19, 2002)*; *In re Lernout & Hauspie Sec. Litig.*, *230 F. Supp. 2d 152 (D. Mass. Aug. 19, 2002)*; *In re Lernout & Hauspie Sec. Litig.*, *286 B.R. 33 (D. Mass. Nov. 18, 2002)*; *Bamberg v. Cowen*, *236 F. Supp. 2d 79 (D. Mass. Dec. 9, 2002)*; *In re Lernout & Hauspie Sec. Litig.*, *236 F. Supp. 2d 161 (D. Mass. Jan. 13, 2003)*.

rized and outstanding stock of Dictaphone, a Delaware corporation. (P 183.)

On May 5, 2000, in what is known as a "reverse triangular merger," L&H acquired all of the outstanding stock of Dictaphone in exchange for approximately 9.4 million shares of L&H common stock through the merger of Dictaphone into a wholly-owned subsidiary of L&H. The merger was effected pursuant to the terms of The Agreement and Plan of Merger dated March 7, 2000 ("Merger Agreement"). Section 2.1 of the Merger Agreement provided that "without any action on the part of any of the holder [sic] of any shares" of Dictaphone, (1) all shares of Dictaphone stock held as treasury stock "shall be cancelled and retired and shall cease to exist" and (2) every other share of Dictaphone common stock "shall be converted into the right to receive" shares of common stock of L&H, and "all such shares of company common stock, when so converted, shall no longer be outstanding and shall automatically be cancelled and retired and shall cease to exist." The L&H subsidiary, Dark Acquisition Corp., survived the merger and changed its name to Dictaphone Corporation ("New Dictaphone"). (P 44.)

The Merger Agreement contained representations and warranties from L&H to Old Dictaphone, including representations concerning the accuracy of filed financial statements. (PP 207-215.) Cowen made face-to-face representations to Old Dictaphone. (PP 218-220, 387.) Old Dictaphone also hired professional advisors, to whom Cowen made representations about the financial condition of L&H. (PP 193-194, 388(i).)

The consideration Old Dictaphone received for its transfer of $ 900 million in assets to L&H, and the assumption of Old Dictaphone's liabilities, were essentially worthless due to the alleged scheme to fraudu-

lently inflate the value of L&H stock. Plaintiff alleges that SG Cowen had participated in this scheme since early 1997. (PP 125-126.)

On November 29, 2000, New Dictaphone filed for relief under Chapter 11 of the United States Bankruptcy Code with the United States Bankruptcy Court for the District of Delaware. (P 45.) On March 13, 2002, the Bankruptcy Court approved the Third Amended Plan of Reorganization and New Dictaphone was discharged from bankruptcy. Pursuant to the Plan, New Dictaphone, as settler, conveyed all its interest in certain pre-merger claims to the Trustee on behalf of the Dictaphone Litigation Trust. (Id.)

The Trustee seeks to recover the "damages suffered by Dictaphone as a result of [the] fraudulent course of conduct." (P 39.) Plaintiff seeks $900 million in damages, which primarily represents the "loss or diminution of its value as a going concern." (P 390.)

III. DISCUSSION

A. Motion to Dismiss Standard

For purposes of this motion, the Court takes as true "the well-pleaded facts as they appear in the complaint, extending [the] plaintiff every reasonable inference in his favor." *Coyne v. City of Somerville, 972 F.2d 440, 442-43 (1st Cir. 1992)* (citing *Correa-Martinez v. Arrillaga-Belendez, 903 F.2d 49, 51 (1st Cir. 1990)*). A complaint should not be dismissed under *Fed. R. Civ. P. 12(b)(6)* unless " 'it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief.' " *Roeder v. Alpha Indus., Inc., 814 F.2d 22, 25 (1st Cir. 1987)* (quoting *Conley v. Gibson, 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957)*).

B. Standing

Vigorously contesting the Trustee's standing under Article III of the Constitution, defendant argues that because there was no purchase of corporate assets as part of the merger, there is no harm to Plaintiff apart from the harm to the shareholders. Neither party contests the shareholders' standing to bring claims arising out of the merger, which have been asserted in the separate litigation.

To have standing, "[a] plaintiff must allege personal injury fairly traceable to the defendant's allegedly unlawful conduct and likely to be redressed by the requested relief." *Raines v. Byrd, 521 U.S. 811, 818, 138 L. Ed. 2d 849, 117 S. Ct. 2312 (1997)* (quoting *Allen v. Wright, 468 U.S. 737, 751, 82 L. Ed. 2d 556, 104 S. Ct. 3315 (1984)).* "The injury alleged must be, for example, distinct and palpable, and not abstract or conjectural or hypothetical. The injury must be fairly traceable to the challenged action, and relief from the injury must be likely to follow from a favorable decision. " *Allen, 468 U.S. at 751* (internal citations omitted).

The threshold issue, then, is the Trustee's standing to pursue the fraud claims on behalf of the bankrupt corporation. "It is well settled that a bankruptcy trustee has no standing generally to sue third parties on behalf of the estate's creditors, but may only assert claims held by the bankrupt corporation itself." *Shearson Lehman Hutton, Inc. v. Wagoner, 944 F.2d 114, 118-19 (2d Cir. 1991)* (citing *Caplin v. Marine Midland Grace Trust Co., 406 U.S. 416, 434, 32 L. Ed. 2d 195, 92 S. Ct. 1678 (1972))* (holding that a claim against a third party for defrauding a corporation with the cooperation of management accrues to creditors, not to the guilty corporation); *In re Rare Coin Galleries of Am., Inc., 862 F.2d 896, 901 (1st Cir. 1988)* ("The trustee steps into the shoes of the

debtor for purposes of asserting or maintaining the debtor's causes of action which become property of the estate.") See generally *Caplin, 406 U.S. at 432 n.21* (rejecting argument that reorganization trustee could bring an action for fraud on behalf of individual debenture holders against indenture trustee, and noting that the trustee may well have interests that differ from those of the bondholders). Thus, to resolve whether the Trustee has standing, the Court must determine what claims the bankrupt corporation could have instituted on the date on which the bankruptcy petition was filed. *Shearson, 944 F.2d at 118.* Here, the bankrupt organization is New Dictaphone.

As a general matter, a bankruptcy trustee has standing to assert those claims of the pre-merger entity that were passed on to the (now bankrupt) corporation that survived the merger. See *8 Del. Code Ann. § 259(a)* ("all property . . . shall be vested in the corporation surviving or resulting from such merger or consolidation"). "The right to a pending cause of action is an asset of a merged corporation which passes to the corporation surviving the merger." *Lewis v. Anderson, 477 A.2d 1040, 1043 (Del. 1984)* (holding that plaintiff who ceases to be a shareholder as a result of merger loses standing to prosecute derivative suit); *Heit v. Tenneco, Inc., 319 F. Supp. 884, 887-88 (D. Del. 1970)* (citing *8 Del. Code Ann. § 259*) (holding that when successive mergers were consummated, all of the claims asserted on behalf of the pre-merger corporation were automatically transferred to the post-merger entity).

This case is much complicated by the fact that the bankrupt corporation was wholly-owned by the alleged perpetrator of the fraud. Can a Dr. Jekyll-and-Mr. Hyde corporation sue itself? Can the trustee of the New Dic-

taphone assert the claims of Old Dictaphone against the New Dictaphone's parent?

1. In Pari Delecto

First, Defendant argues that the action is barred by the doctrine of in pari delecto. See *Mediators, Inc. v. Manney (In re Mediators, Inc.), 105 F.3d 822, 825-26 (2d Cir. 1997)* (holding that the wrongdoing of the sole controlling shareholder must be imputed to the corporation). Courts have consistently held that claims for fraud or misrepresentation perpetrated on investors belong exclusively to those investors to the exclusion of the corporation or its successor in interest, where the corporation itself was involved in the wrongdoing. See *Hirsch v. Arthur Andersen & Co., 72 F.3d 1085, 1094 (2d Cir. 1995)* (holding that the trustee in bankruptcy of the consolidated estate of the company and its general partners lacked standing to bring claims predicated upon the distribution of misleading private placement memoranda to investors in limited partnerships because such claims "are the property of those investors, and may be asserted only by them and to the exclusion of [the trustee]."); *Shearson, 944 F.2d at 118* ("When a bankrupt corporation has joined with a third party in defrauding its creditors, the trustee cannot recover against the third party for damage to the creditors."); *E.F. Hutton & Co., Inc. v. Hadley, 901 F.2d 979, 986-87 (11th Cir. 1990)* (holding that bankruptcy trustee lacks standing to bring claims arising out of Ponzi scheme and that claims belonged only to defrauded investors, and expressing concern for "duplicative litigation"); *Williams v. California 1st Bank, 859 F.2d 664, 666-67 (9th Cir. 1988)* (holding that bankruptcy trustee lacked standing to bring claims against bank arising out of bank's participation in Ponzi scheme on behalf of debtor's creditors, even though

creditors assigned trustee their claims, and noting that "inconsistent actions increase the chance that the Trustee will find her interests diverging from those of the investors on whose behalf she is suing").

Accordingly, the Trustee of the "New" Dictaphone (the wholly-owned subsidiary of the alleged perpetrator of the fraud) has no standing to sue a third party on behalf of the defrauded investors. See *Shearson, 944 F.2d at 120* (holding that when the sole stockholder and decisionmaker of a corporation cooperated with a third party in defrauding the corporation, the claim accrued to creditors "not the guilty corporation."); In *Re Roco Corp., 701 F.2d 978, 984 (1st Cir. 1983)* ("We may impute any fraudulent intent of [the sole shareholder] to the transferor [corporation] because, as the company's president, director and sold shareholder, he was in a position to control the disposition of its property.").

Plaintiff seeks to distinguish this caselaw on the ground that "Old Dictaphone" was not involved in the fraud—indeed was the victim of the fraud—and that its injury is distinct from the shareholders who relied on the specific misrepresentations of the parent company. However, Old Dictaphone cannot arise Phoenix-like to assert pre-merger claims against third parties that New Dictaphone could not assert. "Old Dictaphone" does not have independent standing under Delaware Law because its claims passed on to New Dictaphone.

2. Distinct Injury

Second, even if Old Dictaphone has standing independent of New Dictaphone, defendant argues the Trustee lacks standing because the corporation has asserted no injury distinct from the shareholders. The Trustee argues that the shareholders and the corporate party to a merger

may each have standing to pursue remedies for frauds committed against them.

In certain circumstances, courts have allowed both the shareholders and the successor-in-interest to an entity to pursue claims against third-persons who perpetrated a fraud so long as the individual shareholder has "an injury distinct from the injury to the corporation," and "double recovery is not inherent in plaintiff's theory of the case." *Hayes v. Gross, 982 F.2d 104, 108-09 (3d Cir. 1992)* ("Allowing [stockholders] to pursue this claim [to recover for specific misrepresentations that affected prospective purchaser differently from existing shareholders] will neither prejudice the corporation and its other stockholders nor permit a double recovery for the same injury. If [the bank] has claims against its officers and directors arising from their mismanagement, the [successor-in-interest] is free to pursue those claims for the ultimate benefit of the creditors and stockholders of [the bank].")

With respect to the pre-merger entity, the key inquiry for standing purposes is whether the corporation has suffered an injury distinct from the shareholders. See *Howard v. Haddad, 916 F.2d 167, 170 (4th Cir. 1990)* (holding that the purchasers of a bank stock raised direct, non-derivative claims of misrepresentation against the two directors, stating: "There is no compensable injury to the corporation. . . . The mere fact that Howard and the FDIC are pursuing the same source of assets does not transform Howard's claims into derivative ones."); *Reliance Acceptance Group, Inc. v. Levin (In re Reliance Acceptance Group, Inc.), 235 B.R. 548, 555-56 (D. Del. 1999)* ("Debtors and Shareholders are not . . . pursuing the same cause of action" where "Debtors claim [defendants] defrauded the Company in the split-off transaction" and seek "equitable relief" while "Shareholders

. . . claim the [defendants] defrauded them by publishing false and misleading statements that the shareholders relied on in connection with the purchase or sale of . . . securities" and seek "compensatory damages"); *Greenfield v. Shuck, 867 F. Supp. 62, 67, 73 (D. Mass. 1994)* (permitting the claims of plaintiff purchasers of the subordinated capital notes of a failed bank, and the RTC, the bank's successor-in-interest, to proceed on "equal footing" because the purchasers who received personal assurances had direct, non-derivative claims "sufficiently distinct from any injury to the corporation as a whole").

Delaware law provides guidance on the distinction between injury to the corporation and injury to the shareholders. "A derivative claim is one that is brought by a stockholder, on behalf of the corporation, to recover for harms done to the corporation." *Parnes v. Bally Entm't Corp., 722 A.2d 1243, 1245 (Del. 1999).* A direct claim is one in which an individual stockholder or a class of stockholders seeks "relief for direct injuries that are independent of any injury to the corporation." Id. The Delaware Supreme Court recently clarified the law governing when a stockholder's claim is derivative or direct: "That issue must turn *solely* on the following questions: (1) who suffered the alleged harm (the corporation or the suing stockholders, individually); and (2) who would receive the benefit of any recovery (the corporation or the stockholders, individually)?" *Tooley v. Donaldson, Lufkin, & Jenrette, Inc., 845 A.2d 1031, 1033 (Del. 2004).* "A stockholder who is directly injured . . . does retain the right to bring an individual action for injuries affecting his or her legal rights as a stockholder. Such a claim is distinct from an injury caused to the corporation alone." *Id. at 1036.* The Delaware Supreme Court also emphasized the nature of the duty

owed and the alleged breach. "[A] court should look to the nature of the wrong and to whom the relief should go. . . . The stockholder must demonstrate that the duty breached was owed to the stockholder and that he or she can prevail without showing an injury to the corporation." *Id. at 1039.*

The standing issue turns on whether the Trustee has asserted an injury to the corporation caused by Cowen and whether the corporation would receive the benefit of any recovery. The Amended Complaint seeks $900 million in damages, which primarily represents the loss or diminution of its value as a going concern. The obvious problem with this damage theory is that the "Old Dictaphone" is not a going concern, but ceased to exist after the merger. But even if the Trustee surmounts that hurdle, it must allege a distinct pre-merger injury to the corporation.

The $900 million in damages alleged in the Complaint represents approximately $450 million of shares that Old Dictaphone shareholders exchanged for worthless shares of L&H stock. This represents a distinct loss sustained by the shareholders and any recovery would go to them. While defendant may well have owed a duty to Old Dictaphone under the terms of the Merger Agreement, which it allegedly breached by making intentional misrepresentations, Old Dictaphone would not have the right to recover any diminution in the value of the shares caused by the securities fraud. Therefore, under *Tooley*, and the Article III caselaw on standing, only the shareholders have standing to press the claim for the loss arising from the drop in stock value.

Plaintiff claims that the distinct harm to the corporation is approximately $450 million, the amount that creditors had as a claim on the old corporation which was lost as a result of the merger. The problem with this

argument is that the Trustee can assert only the rights of the corporation, not the rights of the creditors. Moreover, the merger was a benefit to Old Dictaphone because New Dictaphone assumed its debts. See *8 Del. Code Ann. § 259(a)* ("All debts, liabilities and duties of the respective constituent corporations shall thenceforth attach to said surviving or resulting corporation, and may be enforced against it as if said debts, liabilities and duties had been incurred or contracted by it."); *In re Enron Corp., 292 B.R. 507, 514 (S.D.N.Y. 2002)* (holding that Enron Corp. sustained injuries that were "distinct and separate" from injuries sustained by Enron's shareholders as a result of an unconsummated merger where the merger agreement provided that Enron would have benefitted because its debt would have been assumed by the acquirer). Any separate harm to the value of the old corporation as a going concern is speculative given the facts of this case.

ORDER

The Court **ALLOWS** the motion to dismiss (Docket No. 9).

PATTI B. SARIS

United States District Judge

UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

CIVIL ACTION NO. 03-10843-PBS
Filed August 13, 2004

ALAN NISSELSON, TRUSTEE OF THE DICTAPHONE LITIGATION TRUST,
Plaintiff,

—v.—

JO LERNOUT, *et al.*,
Defendant.

MEMORANDUM AND ORDER

Saris, U.S.D.J.

For the reasons stated in this Court's Memorandum and Order dated August 9, 2004 (Docket No. 237), Plaintiff Alan Nisselson, Trustee of the Dictaphone Litigation Trust, lacks standing to bring claims under the federal securities laws, Mass. Gen. Laws ch. 93A, RICO, common law fraud, negligent misrepresentation, conspiracy, and breach of fiduciary duty arising out of the alleged fraudulent scheme at Lernout & Hauspie. Therefore, the Court **ALLOWS** the following Motions to Dismiss: Docket No. 32 (Verbeke); Docket No. 74 (Flanders

Language Valley Fund); Docket No. 76 (Flanders Language Valley Fund Management); Docket No. 94 (KPMG LLP); Docket No. 101 (KPMG-B); Docket No. 103 (Lessius Management Consulting); Docket No. 143 (Mercator Assurances); Docket No. 152 (GIMV).

PATTI B. SARIS

PATTI B. SARIS
United States District Judge

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MASSACHUSETTS

CIVIL ACTION NO. 03-CV-10843 (PBS)
Filed March 25, 2005

ALAN NISSELSON, Trustee of the
Dictaphone Litigation Trust, successor-in-interest
to claims of Dictaphone Corporation,

Plaintiff,

—v.—

JO LERNOUT, *et al.*,

Defendants.

FINDINGS AND ORDER FOR ENTRY OF SEPARATE AND FINAL JUDGMENT FOR DEFENDANT LOUIS-H. VERBEKE

After consideration, the Court finds the following:

FINDINGS

1. The claims in each of the above listed actions allege four different types of fraudulent schemes which led to the collapse of the stock price of Lernout & Hauspie Speech Products (L&H) in the late summer and fall of 2000, spanning three continents, against a

multitude of defendants, including L&H former officers, directors and accountants.

2. On August 13, 2004, in response to S.G. Cowen's Motion to Dismiss, this Court decided that the Plaintiff, Alan Nisselson, Trustee of the Dictaphone Litigation Trust ("Plaintiff"), lacks standing to bring claims under federal securities laws, Mass. Gen. Laws. ch. 93A, RICO, common law fraud, negligent misrepresentation, conspiracy, and breach of fiduciary duty arising out of the alleged fraudulent scheme at Lernout & Hauspie ("Asserted Claims"). This Court's Memorandum and Order of August 13, 2004 ordered dismissal of all claims against S.G. Cowen for lack of standing.

3. Based on its conclusion that Plaintiff lacked standing to bring the Asserted Claims, this Court also dismissed all similar claims against other defendants against whom the Plaintiff had filed Asserted Claims, including Defendant Louis-H. Verbeke ("Verbeke").

4. The legal issue of standing present in this Court's Order dismissing Verbeke is legally distinct from any legal and factual issues remaining before this Court and are unlikely to recur to any significant degree upon appeal.

5. There is unlikely to be any overlap between the issues that could be raised in an appeal of this Court's Order dismissing the claims against Verbeke and the contract issues that remain pending in this Court against other defendants.

6. The parties have not completed discovery in connection with the remaining claims. Resolution of all claims against all parties is a considerable period of time away.

7. Although Verbeke has been dismissed as a defendant pursuant to this Court's Orders, if separate and final judgment is not entered on Plaintiff's Asserted Claims against Verbeke, he will continue to be subject to the expense, burden and uncertainty of being a party to a lengthy and complex litigation in a foreign country.
8. There is no just reason for delaying entry of final judgment against the Plaintiff on its Asserted Claims against Verbeke.

ORDER

Accordingly, the Motion for Entry of Separate and Final Judgment is ALLOWED and final judgment shall enter forthwith dismissing all claims against Louis-H. Verbeke in the above action, with prejudice under U.S. law, for lack of standing.

PATTI B. SARIS

Patti B. Saris
United States District Court Judge

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MASSACHUSETTS

CIVIL ACTION NO. 03-CV-10843 (PBS)
Filed April 4, 2005

ALAN NISSELSON, Trustee of the
Dictaphone Litigation Trust, successor-in-interest
to claims of Dictaphone Corporation,

Plaintiff,

—v.—

JO LERNOUT, *et al.*,

Defendants.

FINDINGS AND ORDER FOR ENTRY OF SEPARATE AND FINAL JUDGMENT FOR MERCATOR AND FOR SIMILARLY SITUATED DEFENDANTS

After consideration, the Court finds the following:

FINDINGS

1. The claims in the above listed action allege fraudulent schemes which led to the collapse of the stock price of Lernout & Hauspie Speech Products (L&H) in the late summer and fall of 2000, against a multi-

tude of defendants, including L&H former officers, directors and accountants.

2. On August 13, 2004, in response to S.G. Cowen's Motion to Dismiss, this Court decided that the Plaintiff, Alan Nisselson, Trustee of the Dictaphone Litigation Trust ("Plaintiff), lacks standing to bring claims under federal securities laws, Mass. Gen. Laws ch. 93A, RICO, common law fraud, negligent representation, conspiracy, and breach of fiduciary duty arising out of the alleged fraudulent scheme at Lernout & Hauspie ("Asserted Claims"). This Court's Memorandum and Order of August 13, 2004 ordered dismissal of all claims against S.C. Cowen for lack of standing.

3. Based on its conclusion that the Plaintiff lacked standing to bring Asserted Claims, the Court also dismissed all similar claims against the other defendants that had filed Motions to Dismiss.

4. The standing issue is factually and legally distinct from the contract issues remaining in the case.

5. There is unlikely to be any overlap between the issues that could be raised in an appeal of this Court's dismissal of the claims against Mercator and similarly situated defendants and the contract issues that will remain pending in this Court against other Deloitte & Touche.

6. The parties have not completed discovery in connection with the remaining claims.

7. If separate and final judgment is not entered on Plaintiff's claims against Mercator, Mercator unnecessarily will continue to be subject to the burden,

expense and uncertainty of being a defendant in complex litigation in a foreign country.

8. There is no just reason for delaying entry of final judgment against the Plaintiff on its claims against Mercator and against similarly situated defendants.

ORDER

Accordingly, Mercator's Motion for Entry of Separate and Final Judgment is ALLOWED and final judgment shall enter forthwith dismissing all claims against Mercator Assurances S.A. and against all other defendants except for Deloitte & Touche, Chase Securities and John H. Duerden in the above action, with prejudice under U.S. law, for lack of standing.

PATTI B. SARIS

Patti B. Saris
Unites States District Court judge

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MASSACHUSETTS

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03 CV 10843 (PBS)
Filed June 7, 2005

ALAN NISSELSON, Trustee of the
Dictaphone Litigation Trust, successor-in-interest
to claims of Dictaphone Corporation,

Plaintiff,

—v.—

JO LERNOUT, *et al.*,

Defendants.

ORDER AND JUDGMENT
AMENDING PRIOR JUDGEMENT

Whereas, the Court having entered an Order directing judgment on April 4, 2005, and

Whereas, the Court did not intend at the time of the entry of the prior Order to enter judgment against Stonington Partners, Inc., Stonington Capital Appreciation 1994 Fund L.P., Stonington Holdings, LLC, Albert J. Fitzgibbons, III, Emil F. Jachmann, Alexis P. Michas, Scott M. Shaw, Joseph O. Skrzypczak, and Peter P. Tong (together the "Former Directors and Shareholders of Old Dictaphone"), but due to the omission of sufficient identification of the parties being dismissed and oversight,

the form of Order proposed and signed provided for a blanket dismissal of all defendants, except for those specifically identified, which inadvertently resulted in dismissal of the Former Directors and Shareholders of Old Dictaphone.

Accordingly, it is hereby ORDERED, pursuant to Fed. R. Civ. P. 60(a), that the Order of April 4, 2005 and Judgment based thereon are hereby amended and modified to the extent inconsistent with this Order, and it is further

ORDERED that Mercator's Motion for Entry of Separate and Final Judgment pursuant to Fed. R. Civ. P. 54(b) is allowed, and final judgment shall enter forthwith dismissing all claims against Jo Lernout, Pol Hauspie, Nico Willaert, Gaston Bastiaens, Carl Dammekens, Ellen Spooren, Ju-Chul Seo, Erwin Vandendriessche, RVD Securities N.V., Dick Cauwelier, Marc G.H. DePauw, Francis Vanderhoydonck, Gerard van Acker, S.ALL. Trust V.Z.W., Flanders Language Valley Fund; Flanders Language Valley Fund Management, Lessius Management Consulting, N.V., Gewestelijke Investeringsmaatschappij Vlaanderen N.V., L&H Investment Company, N.V., Language Investment Company, Language Development Services, Mercator and Noordstar N.V., Language Development Fund; Velstra Pte Ltd., Louis H. Verbeke, Willem Hardeman; Tony Snauwaert, Klynveld Peat Marwick Goerdeler Bedrijfsrevisoven, KPMG LLP, Paul Behets, and SG Cowen Securities Corporation, with prejudice, and without costs for the reasons set forth in my Decision dated August 9, 2004.

PATTI B. SARIS

Patti B. Saris
United States District Court Judge

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

No. 05-1774
Entered: July 7, 2005
Filed: August 8, 2005

ALAN NISSELSON, TRUSTEE OF THE DICTAPHONE LITIGATION TRUST,

Plaintiff, Appellant,

—v.—

JO LERNOUT, ET AL.,

Defendants, Appellees,

CHASE SECURITIES, INC., ET AL.,

Defendants.

ORDER OF COURT

Leave is granted to the district court to enter the June 7, 2005 "Order and Judgment Amending Prior Judgment." Fed. R. Civ. P. 60(a).

By the Court:

Richard Cushing Donovan, Clerk.

BY: MARGARET CARTER
Chief Deputy Clerk.

[certified copies: Hon. Patti B. Saris and Sarah A. Thornton, Clerk]

[cc: Max Folkenflik, Esq., Margaret McGerity, Esq., Karen D. Hurvitz, Esq., Regina Griffin, Esq., Anthony M. Feeherry, Esq., Gus P. Coldebella, Esq., Donald H. Chase, Esq., Edward P. Gilbert, Esq., Gordon Messick Jones, III, Esq., Robert P. Sherman, Esq., Michael P. Connolly, Esq., Ada Fernandez Johnson, Esq., John B. Missing, Esq., David C. Ware, Esq., Thomas J. Gallitano, Esq., John A. Redmon, Esq., Nicholas W. C. Corson, Esq., George A. Salter, Esq., Daniel Curto, Esq., Derek J. T. Adler, Esq., William R. Maguire, Esq., Edward P. Leibensperger, Esq., Charles P. Kindregan, Esq., Gary J. Mennitt, Esq., Alan D. Rose, Esq., James G. McCarney, Esq., Rupinder Hans, Esq., Thomas E. Engel, Esq., Michael L. Chinitz, Esq., Jill Brenner, Esq., Peter E. Gelhaar, Esq., Jonathan K. Cooperman, Esq., Willem Hardeman, Eric Neyman, Esq., Robert J. Kaler, Esq., John Thorpe Richards, Jr., Esq., Robert F. Trout, Esq., Peter B. Krupp, Esq., Diem-Suong T. Nguyen, Esq., Iris Gafni-Kane, Esq., Julian J. Moore, Esq., Michael P. Carroll, Esq., Michael S. Flynn, Esq., Michael L. Simes, Esq., Reshma M. Saujani, Esq., Sean C. Knowles, Esq., Kristin G. McGurn, Esq., Kevin J. Lesinski, Esq., Caroline Press, Esq., Louis M. Solomon, Esq., Michael J. Stone, Esq., Dennis A. Murphy, Esq., Matthew Joseph Matule, Esq., George A. Zimmerman,

Esq., Dalila A. Wendlandt, Esq., Elizabeth Abimbola Thomas, Esq., John D. Donovan, Jr., Esq., Andrew Good, Esq., Steven M. Salky, Esq., Roger E. Zuckerman, Esq., P. Andrew Torrez, Esq., Janet B. Fierman, Esq. and Thomas W. Evans, Esq.]

15 U.S.C. § 78AA

TITLE 15. COMMERCE AND TRADE
CHAPTER 2B. SECURITIES EXCHANGES

§ 78aa. Jurisdiction of offenses and suits

The district courts of the United States and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this title or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this title or rules and regulations thereunder, or to enjoin any violation of such title or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 1254, 1291, 1292, and 1294 of title 28, United States Code. No costs shall be assessed for or against the Commission in any proceeding under this title brought by or against it in the Supreme Court or such other courts.

18 U.S.C. § 1962

TITLE 18. CRIMES AND CRIMINAL PROCEDURE
PART I. CRIMES
CHAPTER 96. RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS

§ 1962. Prohibited activities

(a) It shall be unlawful for any person who has received any income derived, directly or indirectly, from a pattern of racketeering activity or through collection of an unlawful debt in which such person has participated as a principal within the meaning of *section 2, title 18, United States Code* [*18 USCS § 2*], to use or invest, directly or indirectly, any part of such income, or the proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce. A purchase of securities on the open market for purposes of investment, and without the intention of controlling or participating in the control of the issuer, or of assisting another to do so, shall not be unlawful under this subsection if the securities of the issuer held by the purchaser, the members of his immediate family, and his or their accomplices in any pattern or racketeering activity or the collection of an unlawful debt after such purchase do not amount in the aggregate to one percent of the outstanding securities of any one class, and do not confer, either in law or in fact, the power to elect one or more directors of the issuer.

(b) It shall be unlawful for any person through a pattern of racketeering activity or through collection of an unlawful debt to acquire or maintain, directly or indirectly, any interest in or control of any enterprise which

is engaged in, or the activities of which affect, interstate or foreign commerce.

(c) It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

(d) It shall be unlawful for any person to conspire to violate any of the provisions of subsection (a), (b), or (c) of this section.

18 U.S.C. § 1964

TITLE 18. CRIMES AND CRIMINAL PROCEDURE
PART I. CRIMES
CHAPTER 96. RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS

§ 1964. Civil remedies

(a) The district courts of the United States shall have jurisdiction to prevent and restrain violations of section 1962 of this chapter [*18 USCS § 1962*] by issuing appropriate orders, including, but not limited to: ordering any person to divest himself of any interest, direct or indirect, in any enterprise; imposing reasonable restrictions on the future activities or investments of any person, including, but not limited to, prohibiting any person from engaging in the same type of endeavor as the enterprise engaged in, the activities of which affect interstate or foreign commerce; or ordering dissolution or reorganization of any enterprise, making due provision for the rights of innocent persons.

(b) The Attorney General may institute proceedings under this section. Pending final determination thereof, the court may at any time enter such restraining orders or prohibitions, or take such other actions, including the acceptance of satisfactory performance bonds, as it shall deem proper.

(c) Any person injured in his business or property by reason of a violation of section 1962 of this chapter [*18 USCS § 1962*] may sue therefor in any appropriate United States district court and shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee, except that no person may rely upon any conduct that would have been action-

able as fraud in the purchase or sale of securities to establish a violation of section 1962 [*18 USCS § 1962*]. The exception contained in the preceding sentence does not apply to an action against any person that is criminally convicted in connection with the fraud, in which case the statute of limitations shall start to run on the date on which the conviction becomes final.

(d) A final judgment or decree rendered in favor of the United States in any criminal proceeding brought by the United States under this chapter [*18 USCS §§ 1961* et seq.] shall estop the defendant from denying the essential allegations of the criminal offense in any subsequent civil proceeding brought by the United States.

28 USCS § 1254

TITLE 28. JUDICIARY AND JUDICIAL PROCEDURE
PART IV. JURISDICTION AND VENUE
CHAPTER 81. SUPREME COURT

§ 1254. Courts of appeals; certiorari; certified questions

Cases in the courts of appeals may be reviewed by the Supreme Court by the following methods:

(1) By writ of certiorari granted upon the petition of any party to any civil or criminal case, before or after rendition of judgment or decree;

(2) By certification at any time by a court of appeals of any question of law in any civil or criminal case as to which instructions are desired, and upon such certification the Supreme Court may give binding instructions or require the entire record to be sent up for decision of the entire matter in controversy.

28 U.S.C. § 1337

TITLE 28. JUDICIARY AND JUDICIAL PROCEDURE
PART IV. JURISDICTION AND VENUE
CHAPTER 85. DISTRICT COURTS; JURISDICTION

§ 1337. Commerce and antitrust regulations; amount in controversy, costs

(a) The district courts shall have original jurisdiction of any civil action or proceeding arising under any Act of Congress regulating commerce or protecting trade and commerce against restraints and monopolies: *Provided, however,* That the district courts shall have original jurisdiction of an action brought under section 11706 or 14706 of title 49, only if the matter in controversy for each receipt or bill of lading exceeds $ 10,000, exclusive of interest and costs.

(b) Except when express provision therefor is otherwise made in a statute of the United States, where a plaintiff who files the case under section 11706 or 14706 of title 49, originally in the Federal courts is finally adjudged to be entitled to recover less than the sum or value of $ 10,000, computed without regard to any setoff or counterclaim to which the defendant may be adjudged to be entitled, and exclusive of any interest and costs, the district court may deny costs to the plaintiff and, in addition, may impose costs on the plaintiff.

(c) The district courts shall not have jurisdiction under this section of any matter within the exclusive jurisdiction of the Court of International Trade under chapter 95 of this *title [28 USCS §§ 1581* et seq.].

28 USCS § 1367

TITLE 28. JUDICIARY AND JUDICIAL PROCEDURE
PART IV. JURISDICTION AND VENUE
CHAPTER 85. DISTRICT COURTS; JURISDICTION

§ 1367. Supplemental jurisdiction

(a) Except as provided in subsections (b) and (c) or as expressly provided otherwise by Federal statute, in any civil action of which the district courts have original jurisdiction, the district courts shall have supplemental jurisdiction over all other claims that are so related to claims in the action within such original jurisdiction that they form part of the same case or controversy under Article III of the United States Constitution. Such supplemental jurisdiction shall include claims that involve the joinder or intervention of additional parties.

(b) In any civil action of which the district courts have original jurisdiction founded solely on section 1332 of this *title [28 USCS § 1332]*, the district courts shall not have supplemental jurisdiction under subsection (a) over claims by plaintiffs against persons made parties under *Rule 14, 19, 20, or 24 of the Federal Rules of Civil Procedure*, or over claims by persons proposed to be joined as plaintiffs under Rule 19 of such rules, or seeking to intervene as plaintiffs under Rule 24 of such rules, when exercising supplemental jurisdiction over such claims would be inconsistent with the jurisdictional requirements of section 1332 [*28 USCS § 1332*].

(c) The district courts may decline to exercise supplemental jurisdiction over a claim under subsection (a) if—

(1) the claim raises a novel or complex issue of State law,

(2) the claim substantially predominates over the claim or claims over which the district court has original jurisdiction,

(3) the district court has dismissed all claims over which it has original jurisdiction, or

(4) in exceptional circumstances, there are other compelling reasons for declining jurisdiction.

(d) The period of limitations for any claim asserted under subsection (a), and for any other claim in the same action that is voluntarily dismissed at the same time as or after the dismissal of the claim under subsection (a), shall be tolled while the claim is pending and for a period of 30 days after it is dismissed unless State law provides for a longer tolling period.

(e) As used in this section, the term "State" includes the District of Columbia, the Commonwealth of Puerto Rico, and any territory or possession of the United States.

17 CFR 240.10b-5

§ 240.10b-5 Employment of manipulative and deceptive devices.

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.